(1)

No. 96-____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

WILLIAM C. DUNN & DELTA CONSULTANTS, INC.,

Petitioners,

—v.—

COMMODITY FUTURES TRADING COMMISSION,

Respondent,

—v.—

DELTA OPTIONS, LTD. & NOPKINE CO., LTD.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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68 pp

QUESTION PRESENTED

Whether the "Treasury Amendment" (7 U.S.C. § 2(ii)) to the Commodity Exchange Act (7 U.S.C. § 1 *et seq.*) — which provides in pertinent part that "Nothing in this chapter shall be deemed to govern or in any way be applicable to transactions in foreign currency . . . unless such transactions involve the sale thereof for future delivery conducted on a board of trade" — exempts from the jurisdiction of the Commodity Futures Trading Commission off-exchange foreign currency options.

PARTIES TO THE PROCEEDING

Petitioners are William C. Dunn ("Dunn") and Delta Consultants, Inc. ("Consultants"). Dunn is an individual; Consultants is a New Jersey corporation of which Dunn is the president.

Respondents are the Commodity Futures Trading Commission, Delta Options, Ltd. (an investment company incorporated in the Bahamas, which presently is in liquidation), and Nopkine Co., Ltd. (an investment company incorporated in the British Virgin Islands, which has not appeared in this action).

Pursuant to Rules 14.1(b) and 29.6 of the Rules of this Court, petitioner Consultants states that it has no parent companies or subsidiaries.

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MISCELLANEOUS

No. ____

In the

Supreme Court of the United States

October Term, 1995

WILLIAM C. DUNN & DELTA CONSULTANTS, INC.,

Petitioners,

v.

COMMODITY FUTURES TRADING COMMISSION,

Respondent,

v.

DELTA OPTIONS, LTD. & NOPKINE CO., LTD.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners Dunn and Consultants petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit.

OPINIONS BELOW

The opinion of the court of appeals, App. A, is reported at 58 F.3d 50. The order and memorandum of the district court, App. B, are unreported.[1]

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[1] Pursuant to Rule 14.1(h) of the Rules of this Court, federal jurisdiction in the district court was allegedly based on the question of the application of a federal statute. 28 U.S.C § 1331.

JURISDICTION

The judgment of the court of appeals was entered on June 23, 1995. A timely petition for rehearing and a suggestion for rehearing in banc was denied on August 4, 1995. App. C. On December 12, 1995, Justice Ginsburg extended the time for filing a petition for a writ of certiorari to and including January 23, 1996. Petitioners invoke this Court's jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

The "Treasury Amendment" to the Commodity Exchange Act, 7 U.S.C. § 1 *et seq.* (the "CEA"), which is codified at 7 U.S.C. § 2(ii), provides in full as follows:

> Nothing in this chapter shall be deemed to govern or in any way be applicable to transactions in foreign currency, security warrants, security rights, resales of installment loan contracts, repurchase options, government securities, or mortgages and mortgage purchase commitments, unless such transactions involve the sale thereof for future delivery conducted on a board of trade.

STATEMENT

The Treasury Amendment to the CEA exempts from the jurisdiction of the Commodity Futures Trading Commission (the "CFTC") all "transactions in foreign currency," unless they occur on an organized "board of trade" (or "exchange"). 7 U.S.C. § 2(ii). Here, it is undisputed that Petitioners' trading in foreign currency options did not occur on any organized "exchange."

In the district court, the CFTC brought an enforcement action against Petitioners (and the other defendants), and obtained the appointment of a temporary equity receiver. The

district court rejected Petitioners' contention that their off-exchange transactions in foreign currency options were excluded from CFTC jurisdiction by the Treasury Amendment. The court of appeals affirmed.

The 1974 Amendments to the Commodity Exchange Act and the Treasury Amendment

The CEA establishes a comprehensive system for regulating commodity futures contracts[2] and options.[3] It broadly defines a "commodity" (7 U.S.C. § 1(a)(3)), and also provides for broad CFTC authority (*id.* § 2(i)). However, the Treasury Amendment — the immediately following subsection, 7 U.S.C. § 2(ii) — provides an express exemption from CFTC jurisdiction for off-exchange "transactions in foreign currency" (such as those engaged in by Petitioners). This provision — which was inserted into the CEA in 1974 when the CFTC was established as an independent authority — was enacted in response to the specific concerns of the Treasury Department that the exercise of broad jurisdiction by the CFTC over off-exchange foreign currency transactions would adversely impact that market.

The Treasury Department expressed its concern in a letter to the Senate Committee on Agriculture and Forestry, requesting clarification that the CFTC would not have jurisdiction over "futures trading in foreign currencies off organized exchanges." S. REP. No. 1131, 93d Cong., 2d Sess. 49 (1974), *reprinted in* 1974 U.S.C.C.A.N. 5843, 5887.

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[2] A futures contract is an agreement to make or take delivery of a specific amount of a commodity at an agreed-upon price, on a specified future date, which can be traded on a public exchange. JOHN DOWNES & JORDAN ELLIOT GOODMAN, DICTIONARY OF FINANCE & INVESTMENT TERMS 168 (Barron's Financial Guides, 3d ed. 1993).

[3] An option is an agreement that gives the purchaser the right, but not the obligation, to purchase (a "call" option) or to sell (a "put" option) a specified amount of a commodity, at an agreed-upon price, on or before a specified future date. *Id.* at 297-98.

The letter states in pertinent part as follows:

> The Department believes the bills contain an ambiguity that should be clarified. The provisions of the bills do not clearly indicate that the new regulatory agency's authority would be limited to the regulation of futures trading on organized exchanges, and would not extend to futures trading in foreign currencies off organized exchanges. . . .
>
> The Department feels strongly that foreign currency futures trading, other than on organized exchanges, should not be regulated by the new agency. Virtually all futures trading in foreign currencies in the United States is carried out through an informal network of banks and dealers. This dealer market, which consists primarily of the large banks, has proved highly efficient in serving the needs of international business in hedging the risks that stem from foreign exchange rate movements.

Id. at 5887-88.

The Treasury Department also expressed the specific concern that CFTC regulation "would confuse an already highly regulated business sector," and "could have an adverse impact on the usefulness and efficiency of foreign exchange markets for traders and investors." *Id.* at 5888. Accordingly, the letter concluded by "strongly urg[ing] the Committee to amend the proposed legislation" to clarify that it would not apply to "futures trading in foreign currencies or other financial transactions of the nature described above other than on organized exchanges." *Id.* at 5889.

The language which the Treasury Department then proposed was enacted verbatim as the Treasury Amendment (with

a minor excision not relevant in this case). As the Fourth Circuit noted in *Salomon Forex, Inc. v. Tauber,* 8 F.3d 966, 976 (4th Cir. 1993), *cert. denied,* 114 S. Ct. 1540, *reh'g denied*, 114 S. Ct. 2156 (1994), "[t]his Treasury request and direct congressional response is revealing" in its indication of congressional intent to accept the Treasury Department's suggestion that all foreign currency transactions conducted off organized exchanges should be excluded from CEA coverage.

The District Court's Decision

The CFTC alleged that Petitioners (as well as the other defendants) violated the CEA in connection with various investments in off-exchange foreign currency options. On the same day it filed its complaint, the CFTC applied for, and was granted, an *ex parte* order freezing Petitioners' assets.

Subsequently, the CFTC sought the appointment of a temporary equity receiver. In opposition to that request, Petitioners argued that the Treasury Amendment exempted from CFTC jurisdiction off-exchange transactions in foreign currency options such as theirs, and thus the district court was without subject matter jurisdiction. The district court rejected Petitioners' contention, and appointed a temporary equity receiver. App. B.

The Second Circuit's Decision

Although the Second Circuit affirmed, the panel did not consider whether the Treasury Amendment exempts off-exchange foreign currency options from CFTC jurisdiction. Instead, the panel held that it was "foreclosed by clear precedent in this circuit that holds that the term 'transaction in foreign currency' does not include options, even those options traded off-exchange" (App. A, 6a) — citing a decision by a prior panel in *Commodity Futures Trading Commission v. American Board of Trade*, 803 F.2d 1242 (2d Cir. 1986). However, *American Board of Trade*

involved exchange trading of options.[4] Although the court stated that the Treasury Amendment did not "appear to exclude defendants' foreign currency options business from regulation" (*id.* at 1248, emphasis added), it held that options were not "transactions in foreign currency" until they were exercised and currency actually was exchanged — and thus were not exempted by the Treasury Amendment. *Id.* at 1248-49.

The panel below acknowledged Petitioners' and *amici*'s contention that the prior panel's reasoning was dicta because:

> *American Board of Trade* involved transactions that were non-exempt because they had occurred on an exchange. Therefore, it was not necessary [for the prior panel] to hold that all options were outside the Treasury Amendment exemption to reach the conclusion that the transactions at issue in *American Board of Trade* fell within the CFTC's jurisdiction.

App. A, 6a. Although the panel acknowledged that the reasoning of *American Board of Trade* may have been "broader than necessary," it held that it had no authority to reconsider the *ratio decidendi* of a prior panel:

> The fact that a quite different line of reasoning leading to the same result might have been adopted by a prior panel does not give a later panel in this circuit free rein to disregard an earlier decision. . . . Whatever doubts this panel may have about the interpretation given the Treasury Amendment in *American Board of Trade*, therefore, are not grounds for our declining to follow it.

Id.

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[4] Indeed, the defendant was specifically described by the court as "an organization that provided, *inter alia*, an exchange and market place for certain commodity options transactions." 803 F.2d at 1244.

The panel below recognized that, by applying *American Board of Trade* to off-exchange foreign currency options, it created a conflict among the circuit courts, and candidly invited appeal to a higher authority:

> We acknowledge that our interpretation of the phrase "transactions in foreign currency" in *American Board of Trade* conflicts with that of the Fourth Circuit in *Salomon Forex, Inc. v. Tauber*, 8 F.3d 966 (4th Cir. 1993), *cert. denied*, __U.S.__, 114 S. Ct. 1540, 128 L. Ed. 2d (1994). This conflict is for the Supreme Court, not us, to resolve.

Id.

Although the panel below may not have had the authority to limit the breadth of the prior panel's decision in *American Board of Trade*, the court of appeals certainly had that authority in banc. Although Petitioners filed a timely petition for rehearing and suggested rehearing in banc, it was denied. App. C.

REASONS FOR GRANTING THE PETITION

In 1974, at the same time that it expanded the definition of "commodity" and created the CFTC, Congress enacted the "Treasury Amendment" to preserve the historic exemption for off-exchange transactions in foreign currency. The Treasury Amendment is so named because it was proposed by the Treasury Department in an effort to limit the CFTC's regulation of "trading on organized exchanges," and exempt "trading in foreign currencies off organized exchanges," in order to avoid the adverse impact on "the usefulness and efficiency of foreign exchange markets." S. REP. No. 1131, 93d Cong., 2d Sess. 49 (1974), reprinted in 1974 U.S.C.C.A.N. 5843, 5887-88.

The decision of the court below gives the CFTC jurisdiction over options in the multi-trillion dollar off-exchange for-

eign currency market, and squarely conflicts with the decision of the United States Court of Appeals for the Fourth Circuit in *Salomon Forex*. Because of that conflict, parties to foreign currency option contracts are now subject to flatly inconsistent regulations — subject to CFTC jurisdiction in the Second Circuit, and exempt from CFTC jurisdiction in the Fourth Circuit. The consequences of the conflict are not hypothetical. Option contracts governed by New York law are not adjudicated only in the Second Circuit. Indeed, the contracts at issue in *Salomon Forex* were apparently governed by New York law. *See Salomon Forex*, 8 F.3d at 970, 978.

The legal uncertainty created by the lower court's decision jeopardizes the efficiency and future innovation of capital markets, and threatens to increase the cost of government borrowing. As the Department of Justice represented on behalf of the United States and the Securities and Exchange Commission in *Salomon Forex*:

> [F]ailure to qualify for exemption from the CEA under the Treasury Amendment could preclude the existence of certain off-exchange markets which perform vital financial functions, even where they are subject to oversight by other financial regulatory agencies, such as the Department of the Treasury and the SEC.

Brief for the United States as *Amicus Curiae* in *Salomon Forex, Inc. v. Tauber*, No. 92-1406 (4th Cir.), App. D, 7d.

A. *The Judgment of the Court of Appeals Below Conflicts Directly with the Judgment of the United States Court of Appeals for the Fourth Circuit*

The decision below squarely conflicts with a decision of the Fourth Circuit in *Salomon Forex*. There, the Fourth Circuit held that individually negotiated sales of foreign currency futures and options — *i.e.*, off-exchange options — were exempted from CFTC jurisdiction by the Treasury Amendment.

In *Salomon Forex*, a foreign currency trader claimed that his off-exchange transactions in foreign currency forwards and options were voidable as unlawful — since the CEA allegedly required foreign currency futures to be traded exclusively on exchanges designated by the CFTC, and options to be traded on CFTC or SEC designated exchanges. *Salomon Forex*, 8 F.3d at 973. The Fourth Circuit rejected the trader's claim, and found the contracts lawful. Relying on the plain language of the Treasury Amendment, the Fourth Circuit concluded that "transactions in foreign currency" in fact "reach beyond transactions in the commodity itself and . . . include all transactions in which foreign currency is the subject matter, including futures and options," and thus off-exchange "transactions in foreign currency, including futures and options, are exempted from regulation by the CEA." *Id.* at 975-76.

This Court denied a petition for a writ of certiorari filed by the trader in *Salomon Forex*. At that time, there was no direct conflict among the circuits. The Second Circuit, in *American Board of Trade*, had held the Treasury Amendment exemption inapplicable to trading on an organized exchange. The trader in *Salomon Forex*, by contrast, had traded off-exchange. The distinction between on-exchange and off-exchange trading was critical to the Fourth Circuit in *Salomon Forex* (and perhaps to this Court as well), since the Treasury Amendment does not exempt exchange transactions. 7 U.S.C. § 2(ii). As the Fourth Circuit explained:

> Tauber finally relies heavily on decisions of the Second and Seventh Circuits [*Board of Trade of the City of Chicago v. SEC*, 677 F.2d 1137 (7th Cir.), *vacated as moot*, 459 U.S. 1026 (1982)] in defending his position, arguing that affirmance of the district court would result in a split among the circuits. The decisions to which Tauber cites do not conflict with the outcome we reach today, however, as both cases concerned on-exchange trading on behalf of the

> general public, not individual, large-scale deals between professionals.

Salomon Forex, 8 F.3d at 977.[5]

In light of the decision below, the on-exchange/off-exchange distinction by which the Fourth Circuit reconciled its judgment with those of its sister circuits can no longer be maintained. The Second Circuit panel below, on the authority of *American Board of Trade*, has held that the CFTC has jurisdiction over off-exchange foreign currency options and that the Treasury Amendment exemption is inapplicable. By clinging to the prior precedent in *American Board of Trade*, the decision below incorrectly interpreted the "transactions in" language of the Treasury Amendment not to include foreign currency options. However, the plain meaning of the Treasury Amendment was emphasized by the Fourth Circuit in *Salomon Forex*:

> The phrase 'transactions in foreign currency' is broad and unqualified. Its breadth is confirmed by the 'unless' clause which removes from 'transactions in foreign currency' those

[5] Aside from *Salomon Forex*, *American Board of Trade*, and the decision below, the only other appellate court to have addressed, in some fashion, the applicability of the Treasury Amendment to trading in foreign currency options is *Board of Trade of the City of Chicago v. SEC*, 677 F.2d 1137 (7th Cir.), *vacated as moot*, 459 U.S. 1026 (1982). There, during a jurisdictional dispute between the CFTC and the SEC, the Seventh Circuit held that organized exchange trading in options on GNMA securities was within CFTC, rather than SEC jurisdiction. The court specifically stated that it drew "no conclusion as to whether the Treasury Amendment affects any CFTC jurisdiction over options on foreign currency." 677 F.2d at 1154 n.34. Additionally, after the agencies concluded their "CFTC-SEC Jurisdictional Agreement," the decision was vacated as moot. 459 U.S. 1026 (1982). *See also Abrams v. Oppenheimer Gov't Sec., Inc.*, 737 F.2d 582 (7th Cir. 1984) (holding that the Treasury Amendment exempts off-exchange GNMA forward contracts from CFTC jurisdiction).

> transactions which are 'for future delivery conducted on a board of trade.' If Congress meant for the clause 'transactions in foreign currency' to apply only [to] transactions in the commodity itself, it would have no reason to exclude futures transactions conducted on an exchange. The class of transactions covered by the general clause 'transactions in foreign currency' must include a larger class than those removed from it by the 'unless' clause in order to give the latter clause meaning. Thus, because the clause 'unless such transactions involve the sale thereof for future delivery conducted on a board of trade' refers to futures, the general clause 'transactions in foreign currency' must also include futures. Under this analysis, we would have to construe the Treasury Amendment exempting transactions in foreign currency to reach beyond transactions in the commodity itself and to include all transactions in which foreign currency is the subject matter, including futures and options.

Salomon Forex, 8 F.3d at 975-76 (emphasis in original).

Moreover, any interpretation contrary to the Fourth Circuit's analysis would effectively ignore the realities of foreign currency transactions. Both futures and options hedge and/or shift risk, and "it is almost always possible to devise an option with the same economic attributes as a futures contract (and the reverse)." *Chicago Mercantile Exchange v. SEC*, 883 F.2d 537, 543 (7th Cir. 1989), *reh'g denied, en banc*, U.S. App. LEXIS 16,280, *cert. denied*, 496 U.S. 936 (1990). "Since trading in both futures and options involves foreign currency, albeit indirectly, there is no principled reason to distinguish between them in this context." *Salomon Forex*, 8 F.3d at 976. Moreover, if Congress had desired to distinguish between the two types of transactions, it easily could have done so.

Accordingly, there is no valid basis on which to differentiate "options" from other forms of "transactions in foreign currency" — both of which are excluded by the Treasury Amendment. "[A]ll off-exchange transactions in foreign currency, including futures and options, are exempted from regulation by the CEA." *Id.* at 976 (emphasis added).

B. *The Conflict Among the Circuits Subjects Options in the Multi-Trillion Dollar Off-Exchange Foreign Currency Market to Inconsistent Regulation*

The foreign currency options at issue in this case are part of an established international, off-exchange, interbank market in foreign currency. On any given day, hundreds of billions of dollars' worth of currency are bought and sold (by institutional foreign currency banks, dealers, and speculators) and trillions of dollars' worth of foreign exchange contracts are outstanding. *See* Brief of the Foreign Exchange Committee and the New York Clearing House Association as Amici Curiae at 5-6, *CFTC v. Dunn* (2d Cir.). These trades are entered into individually between the participants — with different specifications and duration, and without any involvement of a formally organized "exchange" or "board of trade."

The lack of uniformity among the circuits places the global foreign currency markets in a state of considerable regulatory uncertainty. If the United States, as well as its banking institutions and foreign currency dealers, are to retain their preeminent position in the international currency markets, such conflicts are best resolved by a definitive statement as to the absence of CFTC jurisdiction over such markets. Indeed, CFTC regulation of the off-exchange foreign currency market would reduce efficiency, inhibit innovation in the development of new financial mechanisms, result in higher costs, and damage the United States' ability to compete in the world market. *See Salomon Forex*, 8 F.3d at 974 (citing arguments of *amici*).

Moreover, the Petitioners urge this Court to recognize that the question presented has significant international economic

consequences. The off-exchange foreign currency market, including trading in options, serves a number of fundamental needs of governments and businesses worldwide. The Federal Reserve, as well as various foreign banks, regularly intervene in that market to implement policies relating to their currencies. Additionally, such a market is essential to the smooth functioning of the global trade in goods and services, which often occurs between entities that conduct transactions in more than one currency. Foreign currency options, in particular, are essential to enable businesses and governments to hedge against the risk of adverse exchange rate movements. *See* Brief of the Foreign Exchange Committee and the New York Clearing House Association as Amici Curiae at 4-6, *CFTC v. Dunn* (2d Cir.).

Finally, the importance of the CFTC's lack of jurisdiction with respect to off-exchange foreign currency options is reflected by the interest expressed by various *amici* — in both *Salomon Forex*[6] and in the submissions to the Second Circuit below.[7] It is also anticipated that *amici* submissions will be filed in support of this petition.

C. *The Judgment of the Court of Appeals Below is Inconsistent with the Position of the United States*

The uncertainty created by the decision below is further exacerbated by the opposing governmental positions concerning the lack of CFTC jurisdiction over the off-exchange for-

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[6] In *Salomon Forex* the Treasury Department, the Securities and Exchange Commission, the Foreign Exchange Committee, the Futures Industry Association, and the Managed Futures Association submitted *amicus curiae* briefs arguing that the CEA should not apply to off-exchange foreign currency options.

[7] In the decision below, similar *amicus curiae* briefs were submitted on behalf of the Foreign Exchange Committee, the New York Clearing House Association, the Futures Industry Association, the Managed Futures Association, Credit Lyonnais, Bank Julius Baer & Co. Ltd., and Chase Manhattan Bank, N.A.

eign currency market. Contrary to the CFTC's contentions,[8] the Treasury Department clearly supported the interpretation of the Treasury Amendment in *Salomon Forex* — as stated in the Amicus Brief of the United States:

> [T]he Treasury Department has a strong interest in an efficient market for foreign currency. A smoothly functioning foreign currency market, with a wide range of participants, is essential to international trade and investment flows. However, a narrowed interpretation of the Treasury Amendment could put into question outstanding transactions, as well as inhibit risk-reducing improvements, such as clearing-house operations, in the foreign currency market. The Treasury, as the agency charged with managing the international financial policy of the United States, has an important interest in preventing the legal uncertainty a narrow interpretation of the Treasury Amendment would introduce into this enormous market, which is an essential component of the international economic system.

App. D, 10d.

[8] However, the CFTC itself previously seems to have recognized the proper scope of the Treasury Amendment, when it cited the 1974 Senate Report to confirm that "'regulation by the [CFTC] of transactions in the specified financial instruments . . . is unnecessary, unless executed on a formally organized futures exchange.'" SEC-CFTC Jurisdictional Correspondence, [1975-77 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,117 at 20,834 n.13 (CFTC Staff Response Dec. 3, 1975) (emphasis added). Thus, the CFTC — at least in the past — appears to have recognized that the Treasury Amendment exemption limits its jurisdiction to exchange traded transactions in foreign currency. *See also Statutory Interpretation Regarding Trading in Foreign Currencies for Future Delivery*, 50 Fed. Reg. 42,983, *reprinted in* [1984-86 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,750 (CFTC 1985) (where the CFTC explicitly, albeit begrudgingly, seems to have admitted that at least some foreign currency futures transactions are exempted from the Act's coverage by the Treasury Amendment).

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.[9]

Respectfully submitted,

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January, 1996

[9] Under 28 U.S.C. § 518, Congress has reserved to the Attorney General and the Solicitor General the conduct of litigation in this Court "in which the United States is interested." The Attorney General, in turn, has delegated to the Solicitor General "conducting, or assigning and supervising, all Supreme Court cases, including appeals, petitions for and *in opposition to certiorari*, briefs and arguments, and . . . settlement thereof." 28 C.F.R. § 0.20 (emphasis added). Because the statutory provisions creating the CFTC do not appear to create an exception to the statutory reservation of Supreme Court litigating authority to the Solicitor General (*see* 7 U.S.C. §§ 4a(c), 13a-1(a) & (f)), and the Solicitor General has represented the CFTC in this Court in previous cases (*see Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833 (1986)), we understand that the Solicitor General will represent the United States in this case — including the CFTC. *See Federal Election Comm'n v. NRA Political Victory Fund*, 115 S. Ct. 537, 540-43 (1994). Accordingly, we have not suggested that the Court invite the views of the Solicitor General, since he will presumably file a brief on behalf of the CFTC and the United States. Nevertheless, we have forwarded a courtesy copy of this petition on the General Counsel of the CFTC, who represented respondent CFTC in the court below.

APPENDIX A

Opinion of the
United States Court of Appeals
for the Second Circuit

58 F.3d 50

COMMODITY FUTURES TRADING COMMISSION,
Plaintiff-Appellee,
v.
William C. DUNN and Delta Consultants, Inc.,
Defendants-Appellants
and
Delta Options, Ltd. and Nopkine Co., Ltd.,
Defendants.

No. 856, Docket 94-6197

United States Court of Appeals,
Second Circuit.

June 23, 1995

Before: WINTER, JACOBS, and CABRANES, Circuit Judges.

WINTER, Circuit Judge:

This is an interlocutory appeal from the appointment of a temporary receiver. The principal legal issue is whether the Commodity Futures Trading Commission ("CFTC") has power to regulate off-exchange options involving foreign currencies. Based on a prior decision of this court binding on this panel, we hold that it does and affirm.

BACKGROUND

This is an action by the Commodity Futures Trading Commission against four defendants: (i) William C. Dunn, an in-

dividual and the president and sole shareholder of Delta Consultants; (ii) Delta Consultants, a New Jersey corporation formed by Dunn in 1974; (iii) Delta Options, Ltd., an investment company incorporated in the Bahamas in 1991, to which Dunn is an advisor and of which he was managing director; and (iv) Nopkine Co., Ltd., an investment company incorporated in the British Virgin Islands in 1993, to which Dunn is an advisor.

Beginning in 1992, some of the defendants solicited investments from a number of individuals, partnerships, and companies. These investors understood that Delta Options would use the money to execute investment strategies involving the purchase and sale of call and put options on various foreign currencies. Through these trades, various combinations of sales and purchases of different forms of options created relatively exotic positions in foreign currencies, including "strangles" and "boxes." These trades were done in the name of defendants, and no participations or options were sold directly to investors.

The defendants' trading took place in the so-called off-exchange market. Such trading is over-the-counter and not conducted on any kind of organized exchange. Rather, the market consists of myriad and interlocking contracts struck over the telephone between dealers and through brokers.

According to affidavits submitted by the CFTC, Dunn and his agents, including A.P. Black Limited, an English firm, disseminated false information concerning the risks and rewards of currency trading in general and of investing with defendants in particular. Investors were also deceived as to the success of defendants' trading and the status of the investors' accounts.

Investors in Delta Options received weekly print-outs summarizing the putative current market value of their particular positions. Until late 1993, these print-outs apparently showed impressive returns on the investments. When options expire, the positions are said to "mature." Prior to the maturity of an investor's position, Delta Options would ask the investor whether the investor wanted to "roll over" the positions or to

cash out. By "rolling over" the positions, the investor would reinvest those funds with defendants. Some investors—including those constituting the partnership of Nobad Investment Currency ("Nobad")—claim that misleading print-outs caused them to "roll over" their investments instead of withdrawing them.

The scheme began to unravel in the second half of 1993, and investors began to receive curious communications from defendants. For instance, in early July 1993, investors received a letter from Delta Options to the effect that the "Investment Management Regulatory Organisation Limited," a British regulatory organization, was investigating A.P. Black Limited. In late July 1993, one investor—an English ship repair agency business named Carlden Marine and Industrial Agencies Limited ("Carlden Marine")—was informed by a letter from Delta Options that it would be repaid in full at the next contract maturity dates. Carlden Marine was thus assured that it would be "cashed out" as its positions matured. Over the next two months, however, the monies were not released as anticipated. Funds representing the positions that supposedly matured on August 27, 1993 were sent to Carlden Marine in the middle of October.

Notwithstanding communications from Delta Options and Dunn that alternated between vague and placating, Carlden Marine never received funds corresponding to positions maturing on September 27, 1993. On November 26, Carlden Marine received a letter from Delta Consultants stating that Delta Options had suffered trading losses of $85 million. On November 28, Carlden Marine received a similar communication from Delta Options, except that losses were set at $95 million. Finally, on December 3, 1993, Carlden Marine received a letter from Delta Options that stated that Delta Consultants could not compensate investors for the losses.

Other investors experienced similar difficulties. The Nobad partnership was informed in July through the "Summary Report of Foreign Exchange Option Positions" sent by Delta Consultants that the maturity of some of its currency positions had been extended to late September. They were

then informed in late September that the funds representing such matured positions would not be paid out until November. In late November, the Nobad partners, like Carlden Marine, received communications from Delta Options indicating massive losses and an inability to repay their money.

On the present record, it would appear that, whatever their original intent, defendants became engaged in an old-fashioned "Ponzi" scheme, accompanied by exotic financial vocabulary. The weekly print-outs suggested large returns, which convinced most investors to "roll over" their funds. So long as these funds and money from new investors exceeded losses, any investor who wished to "cash out" could be paid off. The losses, however, were too great to be offset by "rollovers" or new money, and much of the investors' money has disappeared.

At least some money has been transferred to Switzerland. For example, transfer documents from Credit Lyonnais indicate that Delta Options wired $16.5 million from an account in New York to an account in Zurich, Switzerland in July 1993, while documents from Bank Julius Baer reflect a $3 million transfer from a New York account to a Zurich account.

The present lawsuit was commenced by the CFTC on April 5, 1994. On the same date, the CFTC also applied, *ex parte*, for a restraining order, which was promptly entered by the district court, freezing the defendants' assets. On May 4, 1994, the CFTC requested the appointment of a temporary equity receiver. On May 6, the district court held a hearing on this request. Defendants' sole argument at this hearing was that there was no subject matter jurisdiction because the CFTC has no power to regulate options in foreign currency. After a second hearing on June 23, the district court appointed a temporary equity receiver. Appellants brought this interlocutory appeal, along with a motion to stay the order pending appeal. We denied the stay and expedited this appeal.

DISCUSSION

The CFTC's evidentiary proffer sufficiently demonstrated that defendants deceived investors and caused investors to

receive false reports. Such behavior, when undertaken in the course of conduct over which the CFTC has jurisdiction, is unlawful under 7 U.S.C. § 6c(b). The CFTC also has alleged facts sufficient to find Dunn (i) liable for aiding and abetting such violations and (ii) liable for being a controlling person with respect to such violations. *See* 7 U.S.C. § 13c.

The principal question to be addressed, therefore, is whether the CFTC has the power to regulate options in foreign currency. This turns on whether the trading in off-exchange options on foreign currencies is excluded from the CFTC's jurisdiction by the language of the 1974 amendments to the Commodities Exchange Act ("CEA"). The Commodity Futures Trading Commission Act of 1974 created the CFTC and gave it extensive power to regulate futures and options. *See* Pub. L. No. 93-463, 88 Stat. 1389, *et seq.* (1974). However, this authority was circumscribed with respect to foreign currency by the "Treasury Amendment" of 1974, which reads:

> Nothing in this chapter shall be deemed to govern or in any way be applicable to transactions in foreign currency, security warrants, security rights, resales of installment loan contracts, repurchase options, government securities, or mortgages and mortgage purchase commitments, unless such transactions involve the sale thereof for future delivery conducted on a board of trade.

7 U.S.C § 2(ii). The issue is whether or not the phrase "transactions in foreign currency" includes options on foreign currency. If such options are included, then the exemption applies, and the options do not fall within the CFTC's jurisdiction.

This issue is foreclosed by clear precedent in this circuit that holds that the term "transactions in foreign currency" does not include options, even those options traded off-exchange. We addressed this question in *Commodity Futures Trading Commission v. American Board of Trade*, 803 F.2d 1242 (2d Cir. 1986), and interpreted "transactions in foreign currency"

to exclude options. Our reasoning was that an option was simply the right to engage in a transaction in the future, and, until this right matured, there was no exempt "transaction." The exercise of an option would constitute a "transaction in foreign currency," but the purchase or sale of the option itself would not be such a "transaction" under the Treasury Amendment. *Id.* at 1248-49.

Appellants and *amici* urge that this interpretation was dicta because *American Board of Trade* involved transactions that were non-exempt because they had occurred on an exchange. Therefore, it was not necessary to hold that all options were outside the Treasury Amendment exemption to reach the conclusion that the transactions at issue in *American Board of Trade* fell within the CFTC's jurisdiction.

Appellants and *amici* are correct that we could have altered our reasoning and reached the same result by stating that because the instruments at issue in *American Board of Trade* were traded on an exchange they fell outside the Treasury Amendment. Nevertheless, that was not the path we chose. The fact that a quite different line of reasoning leading to the same result might have been adopted by a prior panel does not give a later panel in this circuit free rein to disregard an earlier decision. When a prior decision makes statements in a line of reasoning that are broader than necessary to the affirmance or reversal of a judgment, a later panel may confine the precedential effect to a narrower ground within the line of reasoning. However, a later panel may not disregard the reasoning of a decision because an entirely different line of reasoning was available. Whatever doubts this panel may have about the interpretation given the Treasury Amendment in *American Board of Trade*, therefore, are not grounds for our declining to follow it. We acknowledge that our interpretation of the phrase "transactions in foreign currency" in *American Board of Trade* conflicts with that of the Fourth Circuit in *Salomon Forex, Inc. v. Tauber*, 8 F.3d 966 (4th Cir. 1993), *cert. denied*, ___ U.S. ___, 114 S. Ct. 1540, 128 L.Ed.2d (1994). This conflict is for the Supreme Court, not us, to resolve.

Amici warn of a number of potentially dire effects that could result from a holding that off-exchange currency options fall within the subject matter jurisdiction of the CFTC. These dire effects are to a degree deflected by the CFTC's trade option exemption. *See* 17 C.F.R. § 32.4 (limited exemption for commodity options "offered by a person which has a reasonable basis to believe that the option is offered to a producer, processor, commercial user or merchant . . . solely for purposes related to its business as such"). At oral argument, for example, the CFTC represented that the trade option exemption would apply to options in foreign currency traded among banks. In any event, we are bound by precedent.

We have examined appellants' claim that the district court abused its discretion by appointing a temporary receiver. We hold that Judge Griesa's actions were proper and responsible under the circumstances, and appellants' contentions to the contrary are without merit.

Affirmed.

APPENDIX B

Order Appointing Temporary Equity Receiver

COMMODITY FUTURES TRADING COMMISSION,
Plaintiff,
v.
William C. DUNN, Delta Consultants, Inc.,
Delta Options, Ltd., and Nopkine Co. Ltd.,
Defendants.

94 Civ. 2403 (TPG)

United States District Court
for the Southern District of New York

June 23, 1994

WHEREAS, Plaintiff Commodity Futures Trading Commission having applied for an Order of this Court appointing a temporary equity receiver in the above-captioned case, and this Court having considered said application and arguments thereon and being fully advised in the premises:

Accordingly, it is HEREBY ORDERED that Michael S. Sackheim is appointed as the Temporary Equity Receiver ("Receiver") and, in such capacity, is authorized:

(1) To take immediate custody, control and possession of the assets and property belonging to, or in the possession, custody or control of, Defendants William C. Dunn, Delta Consultants, Inc., Delta Options, Ltd. ("Delta Options") and Nopkine Co. Ltd. (hereinafter collectively referred to as "the Defendants"), including, but not limited to, books and records of account and original entry, computer and other electronically stored and sorted data, funds, securities, commodity accounts, bank and trust deposit accounts, real and personal property, premises, contents of safety deposit boxes, precious metals, currencies, coins and any other assets or property, wheresoever situated;

(2) To collect and take charge of, hold and administer forthwith all such assets and property subject to further Order of this Court, in order to prevent irreparable loss, damage and injury to customers of said Defendants and to conserve, and prevent the dissipation of, funds;

(3) To locate, freeze, marshal, recover and preserve forthwith all of the assets and property of said Defendants, wheresoever situated, for the benefit of the Defendants' customers, and to make an accounting thereof to this Court; and

(4) To have such other and further powers as this Court, from time to time, may direct.

It is FURTHER HEREBY ORDERED:

(5) That the Receiver shall cooperate in a reciprocal manner, including the reciprocal sharing of such information and documents as may be appropriate and lawful, with Messrs. Macgregor Robertson and Anthony Kikivarakis, in their capacity as the Joint Official Liquidators of Defendant Delta Options in the proceeding captioned *In the Matter of Delta Options Limited and In the Matter of the International Business Companies Act, 1989*, now pending in the Supreme Court of the Commonwealth of the Bahamas, so as to reduce or eliminate any unnecessary duplication of effort and unnecessary expenditure of resources;

(6) That, upon application to, and approval by, this Court, with notice to all parties, Messrs. Macgregor Robertson and Anthony Kikivarakis may be compensated for reasonable disbursements, fees and ex-

penses which they have incurred to date as the Joint Official Liquidators of Defendant Delta Options in *In the Matter of Delta Options Limited and In the Matter of the International Business Companies Act, 1989*, from assets and property of Defendant Delta Options which have been frozen or recovered in this action to date;

(7) That, upon application to, and approval by, this Court, with notice to all parties, the Receiver, and any persons retained by him to assist in performing any of the activities authorized herein, may be compensated for reasonable disbursements, fees and expenses from the assets and property of the Defendants in this action;

(8) That nothing in this Order shall be deemed to prevent Messrs. Macgregor Robertson and Anthony Kikivarakis, as the Joint Official Liquidators of Defendant Delta Options in *In the Matter of Delta Options Limited and In the Matter of the International Business Companies Act, 1989*, from performing their obligations to the Supreme Court of the Commonwealth of the Bahamas, including locating, freezing, marshalling, recovering and preserving assets which they reasonably believe belong to Defendant Delta Options, provided that all such assets, wheresoever located, shall be subject to all outstanding Orders issued by this Court, including, but not limited to, this Court's *Ex Parte Restraining Order*, dated April 5, 1994, except as otherwise provided herein;

(9) That any assets which are located, frozen, marshalled, recovered or preserved by the Receiver or by Messrs. Macgregor Robertson and Anthony Kikivarakis, in their capacity as the Joint Official Liquidators of Defendant Delta Options in *In the Matter of Delta Options Limited and In the Matter*

of the International Business Companies Act, 1989 and are reasonably believed to belong to Defendant Delta Options, shall not be distributed to customers, investors or creditors of Delta Options, unless such distribution has been duly approved by this Court and by the Supreme Court of the Commonwealth of the Bahamas; provided that assets belonging to any of the other Defendants in this action are, and shall remain, subject to this Court only; and

(10) That, except as otherwise provided herein, all outstanding Orders issued by this Court in this action, including, but not limited to, the Stipulation and Order filed on April 20, 1994 and agreed to by the Commission and Defendants William C. Dunn and Delta Consultants, Inc., shall remain in full force and effect, until further notice from this Court.

Done and Ordered at New York, New York, on this 23rd day of June, 1994.

Thomas P. Griesa

THOMAS P. GRIESA
UNITED STATES DISTRICT
JUDGE

MEMORANDUM

COMMODITY FUTURES TRADING COMMISSION,
Plaintiff,
v.
William C. DUNN, Delta Consultants, Inc., Delta Options, Ltd., and Nopkine Co. Ltd.,
Defendants.

94 Civ. 2403 (TPG)

United States District Court
for the Southern District of New York

July 1, 1994

On June 24, 1994 the court held a hearing on plaintiff's application for the appointment of a receiver. The arguments for and against the receivership had also been discussed on at least one earlier occasion. On June 24 the court granted plaintiff's application and signed an order appointing the receiver.

The principal opponents of the receivership application were defendants William C. Dunn and Delta Consultants, Inc., represented by Gary D. Stumpp, Esq. Among other things, Mr. Stumpp has contended that the court lacks subject matter jurisdiction in this case. At the June 24 hearing the court stated that it has jurisdiction, and further stated that a formal opinion to that effect would be filed shortly.

In so stating, the court overlooked the fact that on June 15 Mr. Stumpp filed a motion to dismiss the complaint for lack of subject matter jurisdiction and that this motion is returnable on August 10. Plaintiff has not yet responded to this motion.

The court wishes to revise what it said on June 24 with reference to jurisdiction. The court will not issue a formal ruling on jurisdiction until the submissions have been com-

pleted on Mr. Stumpp's motion. Plaintiff should, of course, respond to that motion. However, the court does state that it is sufficiently satisfied on the subject of jurisdiction so that it believes that the appointment of a receiver is proper. The court relies on *Commodity Futures Trading Commission v. The American Board of Trade, Inc.*, 803 F.2d 1242, 1248 (2d Cir. 1986).

Dated: New York, New York
July 1, 1994

Thomas P. Griesa

THOMAS P. GRIESA
U.S.D.J.

APPENDIX C

Order of the
Second Circuit Court of Appeals
Denying Petition for
Rehearing and Suggestion for
Rehearing In Banc

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT
UNITED STATES COURT HOUSE
40 FOLEY SQUARE
NEW YORK 10007

GEORGE LANGE III
CLERK

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, Foley Square, in the City of New York, on the 25th day of September one thousand nine hundred and ninety-five.

CFTC

v · Dkt No: 94-6197

Dunn

A petition for rehearing containing a suggestion that the action be *reheard* in banc having been filed herein by the appellants WILLIAM C. DUNN and DELTA CONSULTANTS, INC.

Upon consideration by the panel that decided the appeal, it is Ordered that said petition for rehearing is **DENIED**.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges for the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereof.

FOR THE COURT:
GEORGE LANGE III, CLERK
Arthur M. Heller 9/22/95
By: Arthur M. Heller, Date
Administrative Attorney

APPENDIX D

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE IN *SALOMON FOREX, INC. V. TAUBER*, NO. 92-1406 (4th Cir.)

IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

SALOMON FOREX, INC.,

Plaintiff-Appellee,

v.

LASZLO N. TAUBER, M.D.,

Defendant-Appellant,

LASZLO N. TAUBER, M.D.,

Third-Party Plaintiff-Appellant,

v.

SALOMON BROTHERS, INC., *et al.*,

Third-Party Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA

BRIEF FOR THE UNITED STATES AS *AMICUS CURIAE*

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IN THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 92-1406

SALOMON FOREX, INC.,

Plaintiff-Appellee,

v.

LASZLO N. TAUBER, M.D.,

Defendant-Appellant,

LASZLO N. TAUBER, M.D.,

Third-Party Plaintiff-Appellant,

v.

SALOMON BROTHERS, INC., *et al.*,

Third-Party Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA

BRIEF FOR THE UNITED STATES AS *AMICUS CURIAE*

STATEMENT OF INTEREST OF THE UNITED STATES

On October 23, 1974, the Commodity Exchange Act, 7 U.S.C. 1, *et seq.* ("CEA"), was amended by the Commodity Futures Trading Commission Act of 1974, Pub. L. 93-463, 88 Stat. 1389, *et seq.* ("CFTCA"). The CFTCA broadened the definition of commodities in the CEA to include, in addition to various previously *enumerated* agricultural products,

> all other goods and articles, except onions as provided in Public Law 85-839, and all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in . . . .

Sec. 201(b), Pub. L. 93-463, 88 Stat. 1395. In addition, the CFTCA created the Commodity Futures Trading Commission ("CFTC"), which assumed the regulatory powers previously exercised by the Secretary of Agriculture in regard to trading in commodity futures contracts.

While the 1974 amendments resulting in the CFTCA were being considered, the Treasury Department proposed to Congress that certain transactions in certain financial instruments be exempted from coverage of the CEA, and, therefore, from the regulatory authority of the CFTC. *See, e.g.*, S. Rep. No. 1131, 93rd Cong., 2d Sess., 49 - 51 (1974). With one exception not relevant here, Congress adopted the Treasury Department's proposal, promulgating as part of the CEA what is now known as the "Treasury Amendment." The Treasury Amendment provides, in relevant part:

> Nothing in this Act shall be deemed to govern or in any way be applicable to transactions in foreign currency, security warrants, security rights . . . [or] government securities, . . . unless such transactions involve the sale thereof for future delivery conducted on a board of trade.

Sec. 201(b), Pub. L. 93-463, 88 Stat. 1395.

In this case, the district court has reasoned that "well-established principles of statutory interpretation compellingly point to the conclusion that the [subject] contracts between [defendant and plaintiff] are covered by the Treasury Amendment and thus excluded from regulation under the CEA," Joint Appendix ("J.A.") 50, finding that

> the phrase "transactions in foreign currency" [in the Treasury Amendment] plainly and un-

> ambiguously means any transaction, without limitation as to the participants involved, in which foreign currency is the commodity or subject matter . . . .

Ibid. Accordingly, the district court concluded:

> All transactions in which foreign currency is the actual subject matter of an off-exchange contract for future delivery are exempt from the CEA.

J.A. 56 - 57.

The exclusivity provision and exchange-trading requirement of the CEA confer upon the CFTC exclusive jurisdiction with respect to contracts of sale of a commodity for future delivery and certain other commodity instruments, and makes it illegal to trade futures unless the contract is executed on a designated contract market.[1] Thus, failure to qualify for exemption from the CEA under the Treasury Amendment could preclude the existence of certain off-exchange markets which perform vital financial functions, even where they are subject to oversight by other financial regulatory agencies, such as the Department of the Treasury and the SEC. The United States Department of the Treasury and the Securities and Exchange Commission ("SEC") have important interests in the preservation of the reach of the district court's interpretation of the Treasury Amendment in this case.

* * * * *

A narrowing, or reversal, of the district court's decision would create legal uncertainty which could have an adverse impact upon the market for Treasury securities, and markets for other government securities, as well as on the market for foreign currencies. In addition, narrowing or reversal could produce detrimental limitations on the types of securities the

[1] *See* 7 U.S.C. 2, 6(a).

Treasury, and other issuers of government securities, could market in the future.

In particular, the Treasury Department is concerned that a more narrow interpretation of the Treasury Amendment in this case would create legal uncertainty for the "when-issued" market for Treasury securities — a crucial part of the distribution and pricing mechanism for marketable Treasury securities at original issuance.

"When-issued" trading consists of agreements, entered into between participants in the Treasury securities market, to purchase and sell Treasury securities prior to their issuance, at an agreed upon yield or price. Ordinarily, when-issued trading is conducted between the date of the announcement by the Treasury Department of a scheduled auction of a security, and the settlement — or issuance — date for that security.[2] In recent years, the Treasury Department has conducted over 150 auctions each year, and, on any given day, several different Treasury issues may be the subject of trades on the when-issued market, with a substantial volume being traded.

When-issued trading fulfills several crucial functions in the primary distribution process for Treasury securities. First, it serves as an important price discovery mechanism for a security to be auctioned, allowing auction participants to bid more confidently. When-issued trading also reduces informational advantages, and inequalities of informational access, among potential bidders in the auctions, and provides auction participants the opportunity to hedge positions acquired in the auction. Finally, the availability of when-issued trading

[2] Delivery of the securities subject to when-issued trades takes place on the issuance date of the security. In some instances, the need for actual delivery of the securities is eliminated by the parties' entering into offsetting when-issued transactions. In addition, when-issued transactions between netting members of the Government Securities Clearing Corporation ("GSCC") are settled on a net basis. The GSCC membership comprises primarily the interdealer market. As GSCC becomes the counterparty to all transactions which it nets, it subjects when-issued, and other trades which create market exposure for GSCC, to daily margining requirements.

significantly increases flexibility in the timing of Treasury securities purchases for portfolio managers and other large investors, by offering an alternative to their bidding directly in auctions. Available data suggest that a significant portion of an offering of Treasury securities is sold to final investors before the auction. When-issued trading offers these important ultimate purchasers a mechanism for avoiding the potential price and quantity risks of auction bidding.

For these reasons, the smooth functioning of the when-issued market in Treasury securities contributes directly to the success and to the fairness of the auctions. This increases the overall liquidity and efficiency of the Treasury securities market, and contributes to the financing of the federal debt at the lowest possible cost to the Treasury, and ultimately to the taxpayer. The affirmation by the district court in this case that the Treasury Amendment would exempt from coverage of the CEA "all transactions" in the instruments enumerated in the Treasury Amendment essentially protects these several interests the Treasury Department has in the government securities market.

A narrower interpretation of the Treasury Amendment in this case could have adverse impact on matters of concern to the Treasury Department, beyond the deleterious impact upon the present market for Treasury securities. Such an interpretation could inhibit market innovation in the development of new mechanisms for trading government securities, and could reduce the flexibility in the development of new types of Treasury securities. These restrictions could, in turn, reduce market efficiency for Treasury securities and other government securities in the future, thereby increasing the cost of financing.[3]

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[3] For example, the Treasury might, in the future, determine that it would be advantageous to issue securities which are indexed to the price of a commodity. A narrow interpretation of the Treasury Amendment could preclude trading such a security in the over-the-counter market, or could even preclude the Treasury from issuing such a security, if the structure of the security meant that it was viewed as an instrument governed by the CEA.

In addition to being the issuer of the public debt, and having important interests in the smooth functioning of the government securities market, which minimizes the government's financing costs, the Treasury Department has an interest in this case stemming from its role as rulemaker for government securities brokers and dealers under the Government Securities Act of 1986 ("GSA").[4] A narrow interpretation of the Treasury Amendment, which would create legal uncertainties with regard to transactions in the government securities market, could engender further, and detrimental, confusion about the Treasury's authority to regulate government securities brokers and dealers with respect to such transactions.

Finally, the Treasury Department has a strong interest in an efficient market for foreign currency. A smoothly functioning foreign currency market, with a wide range of participants, is essential to international trade and investment flows. However, a narrowed interpretation of the Treasury Amendment could put into question outstanding transactions, as well as inhibit risk reducing improvements, such as clearinghouse operations, in the foreign currency market. The Treasury, as the agency charged with managing the international financial policy of the United States, has an important interest in preventing the legal uncertainty a narrow interpretation of the Treasury Amendment would introduce into this enormous market, which is an essential component of the international economic system.

Thus, any narrowing of the exclusionary coverage of the Treasury Amendment as pronounced by the district court —

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[4] Pub. L. 99-571, 100 Stat. 3208 (1986). The GSA established a federal system for the regulation of the government securities market, including previously unregulated brokers and dealers. *See generally*, Department of the Treasury, Securities and Exchange Commission, and Board of Governors of the Federal Reserve System, *Study of the Effectiveness of the Implementation of the Government Securities Act of 1986*, pp. 1-3 (October 1990) (describing regulation of government securities market). Treasury's rulemaking authority lapsed on October 1, 1991; however, legislation is pending to renew it.

including the imposition of a limitation based upon the identity of a participant — would have a detrimental impact upon these several markets, and would create significant uncertainty among market participants.

* * * * *

The Securities and Exchange Commission advises us that it supports the positions of the United States in this case. The SEC is the agency responsible under the federal securities laws for regulation of transactions in securities and options "on any security . . . or group or index of securities (including any interest therein or based on the value thereof)," and for the administration and enforcement of those laws.[5] The SEC's regulation of trading in these securities and options involves oversight of securities exchanges and off-exchange (over-the-counter) markets, as well as market professionals and intermediaries such as securities broker-dealers (including government securities dealers) and securities and option clearing agencies (including clearing agencies which clear and settle trades in government securities, options on U.S. Treasury securities, and options on foreign currency).

The scope of the Treasury Amendment's statutory exclusion from the CEA encompasses transactions in a variety of securities, such as "security warrants," "security rights," and "government securities."[6] The Court's interpretation of the Treasury Amendment in this case will have a direct impact

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[5] *See* Section 9(g) of the Securities Exchange Act, 15 U.S.C. 78i(g) ("Exchange Act"). Options relating to foreign currency traded on a national securities exchange are defined as "securities" for the purposes of the Exchange Act. *See* 15 U.S.C. 78c(a)(10). The Exchange Act confers on the SEC jurisdiction over such trading, 15 U.S.C. 78i(g), and such trading is expressly excluded from the coverage of the CEA. *See* 7 U.S.C. 6c(f).

[6] The SEC shares regulatory authority with respect to the trading of government securities with the Treasury Department and federal financial institution regulatory authorities. *See generally*, Study, *supra*, n.4.

on the Amendment's application to off-exchange trading of all instruments enumerated in the Amendment. Accordingly, the interpretation will have important consequences for the SEC's regulatory jurisdiction as related to securities and securities-derivative products as comprehended within the Amendment, and for market participants subject to SEC oversight.

The SEC's regulatory jurisdiction with respect to certain securities-derivative products was expressly clarified by Congress in 1982 and 1983 through enactment of the SEC-CFTC Accord, which resolved certain jurisdictional disputes between the SEC and the CFTC with respect to options on securities and other securities-derivative products.[7] Taken together, the Accord Amendments and the earlier enacted Treasury Amendment represent a comprehensive jurisdictional scheme adopted by Congress in consultation with the regulatory agencies affected.

The SEC has a strong interest in ensuring proper interpretation of the Treasury Amendment to clarify the CEA's applicability to securities and securities-derivative products regulated by the SEC. Narrowing the exclusionary coverage of the Treasury Amendment, as urged by defendant (and thereby expanding the potential sweep of the CEA exclusivity provision), has a serious potential for disrupting securities markets, and for causing uncertainty and confusion for market participants.

* * * * *

For these reasons, the United States has a strong and important interest in having this Court affirm the district court's interpretation of the Treasury Amendment.

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[7] *See* Act of Oct. 13, 1982, Pub. L. No. 97-303, 96 Stat. 1409 (amending the federal securities laws); Act of Jan. 11, 1983, Pub. L. No. 97-444, 96 Stat. 2294 (amending the CEA).

STATEMENT OF THE ISSUE PRESENTED FOR REVIEW

Although appellant presents additional issues for this Court's review, this brief addresses only the following issue:

> Whether the district court properly held that the foreign currency trading contracts entered into between plaintiff and defendant herein are exempt from regulation under the Commodity Exchange Act, as amended, 7 U.S.C. § 1, *et seq.* (1980 & Supp. 1992).

STATUTORY PROVISION INVOLVED

7 U.S.C. § 2 provides, in relevant part:

> . . . . Nothing in this chapter shall be deemed to govern or in any way be applicable to transactions in foreign currency, security warrants, security rights, resales of installment loan contracts, repurchase options, government securities, or mortgages and mortgage purchase commitments, unless such transactions involve the sale thereof for future delivery conducted on a board of trade. The term "future delivery," as used in this chapter, shall not include any sale of any cash commodity for deferred shipment or delivery.

STATEMENT OF THE CASE[8]

This case arises out of a protracted series of transactions between plaintiff, Salomon Forex, Inc., a prominent foreign currency trading company, and defendant, Laszlo Tauber.

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[8] This statement is limited to matters which are relevant to the issue which *amicus* will address.

Defendant is a general surgeon with an active practice in Northern Virginia, who is also both a major real estate investor, owning a 75% interest in a company which is one of the federal government's largest private landlords, and a major foreign currency trader. J.A. 40-41.[9] Since 1981, defendant has engaged in billions of dollars of foreign currency trading, involving at least 14 well-known companies, including his wholly-owned foreign currency trading company which has a seat on the nation's largest foreign currency exchange. *Ibid.*

As described by the district court, plaintiff and defendant executed off-exchange futures and options contracts. J.A. 42.[10] These contracts were secured by defendant with various forms of collateral; however, plaintiff ultimately sought greater collateral from defendant, which defendant agreed to deliver, but did not, causing plaintiff to decline to enter any further contracts, and to permit the existing contracts to mature. J.A. 44. Upon maturation, defendant's collateral was worth over $20 million less than the amount due plaintiff, and plaintiff brought this action to recover the difference. *Ibid.* Relevant to this matter was the defense that the subject transactions, which were not conducted on or subject to the rules of a board of trade designated by the CFTC as a contract market for trading futures contracts in the commodity involved, were illegal contracts under the CEA, and, therefore, unenforceable.[11] Plaintiff, however, contended that the transactions were governed by the Treasury Amendment, and, therefore, not subject to the CEA.

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[9] The district court suggests that defendant's net worth is in excess of half a billion dollars. J.A. 41.

[10] The "futures" contracts — which may have been "cash forward" contracts, within the meaning of 7 U.S.C. § 2, which are exempted from the CEA (*ibid.*) — were for purchase or sale on a specific future date of a specified amount of currency at an agreed price; the option contracts consisted of purchasing the right to buy or sell a specific amount of foreign currency in the future at an agreed price.

[11] *See* 7 U.S.C. § 6.

The district court agreed with plaintiff. Properly starting with "the language of the statute itself," J.A. 49, the court reasoned that "well-established principles of statutory interpretation compellingly point to the conclusion that the [subject] contracts between Tauber and Salomon Forex are covered by the Treasury Amendment and thus excluded from regulation under the CEA." J.A. 50. Accordingly, the district court held that

> the phrase "transactions in foreign currency" [in the Treasury Amendment] plainly and unambiguously means any transaction, without limitation as to the participants involved, in which foreign currency is the commodity or subject matter . . . .

Ibid.

The district court rejected defendant's argument that legislative history established a limitation upon the participants, observing that the Amendment's "plain language is not qualified in any respect to limit the covered participants," J.A. 51, and that the legislative history, "taken as a whole . . . reveals no clear and unambiguous expression of legislative intent," J.A. 53, to limit the covered participants. *Ibid.* Accordingly, the district court concluded that

> [a]ll transactions in which foreign currency is the actual subject matter of an off-exchange contract for future delivery are exempt from the CEA.

J.A. 56-57.

Amicus will address only the issue of the reach and coverage of the Treasury Amendment, as defined by the district court.

STANDARD OF REVIEW

The proper interpretation of a statute as required by the issue here is purely a question of law, which is reviewed *de novo* by this Court. *See Basch* v. *Westinghouse Electric Corporation*, 777 F.2d 165, 169 n.5 (4th Cir. 1985).

ARGUMENT

THE DISTRICT COURT CORRECTLY INTERPRETED THE TREASURY AMENDMENT

1. The district court correctly followed the applicable canons of statutory construction.

The district court correctly interpreted the Treasury Amendment, pronouncing that

> the phrase "transactions in foreign currency" [in the Treasury Amendment] plainly and unambiguously means any transaction, without limitation as to the participants involved, in which foreign currency is the commodity or subject matter . . . .

J.A. 50. Further, the district court concluded that, whether structured as a future contract or an option,

> [a]ll transactions in which foreign currency is the actual subject matter of an off-exchange contract for future delivery are exempt from the CEA.

J.A. 56-57. In so interpreting the statute, the district court properly was governed by the "familiar canon of statutory construction,"

> the starting point for interpreting a statute is the language of the statute itself. Absent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive.

Consumer Product Safety Commission v. *GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980); *and see Russello* v. *United States*, 464 U.S. 16, 20 (1983); Jt. App. 49-50.

In this case, "the language of the statute itself" unqualifiedly excludes from coverage of the CEA "transactions in foreign currency, [*etc.*], unless such transactions involve the sale thereof for future delivery conducted on a board of trade." 7 U.S.C. § 2. Therefore, "absent a clearly expressed legislative intention to the contrary," the district court could only conclude, as it did, that transactions in foreign currency are excluded from the CEA "without limitation as to the participants involved." Jt. App. 50.

According to the "time-honored" rule, "when the language of a statute is clear, there is no need to rely on its legislative history."[12] Nonetheless, the district court went further, and correctly demonstrated that nothing in the legislative history of the Treasury Amendment can be interpreted as a "clearly expressed legislative intention" to create a limitation "as to the participants involved." First,

> in a letter to the [Senate] Committee [on Agriculture and Forestry] dated July 30, 1974, the Department of Treasury recommended that a provision be included in the legislation [to become the CFTCA] exempting, from regulation by the Commission, foreign currency futures trading other than on organized exchanges.

S. Rep. No. 93-1131, 93d Cong., 2d Sess. 49 (1974). Further, the letter to the Committee concluded with Treasury's "strongly urg[ing]" the Committee to

> amend the proposed legislation to make clear that its provisions would not be applicable to futures trading in foreign currencies or other

[12] *First United Methodist Church* v. *U.S. Gypsum Co.*, 882 F.2d 862, 865 (4th Cir. 1989), *cert. denied*, 493 U.S. 1070 (1990), citing *Ex Parte Collett*, 337 U.S. 55, 61 (1949).

> financial transactions of the nature above other than on organized exchanges.

Id. at 51.

What is most important about this "provision," which was enacted as the "Treasury Amendment," with only a minor change, not relevant here,[13] as the district court correctly observed, is that its "plain language is not qualified in any respect to limit the covered participants." Jt. App. 51. Accordingly, the inquiry can properly stop at this point, since "[l]egislative history is irrelevant to the interpretation of an unambiguous statute." *In re Moore*, 907 F.2d 1476, 1479 (4th Cir. 1990), quoting *Davis* v. *Michigan Department of Treasury*, 489 U.S. 803, 808 - 809 n. 3 (1989).

Moreover, further investigation into the legislative history does not reveal "a clearly expressed legislative intention to the contrary," *Consumer Product Safety Commission*, *supra*, 447 U.S. at 108, sufficient to permit passing over the unambiguous language of the statute. As the district court pointed out, the legislative history suggests nothing other than a combination of factors and goals comprehended in the enactment of the Treasury Amendment. *See, e.g.*, S.Rep. No. 1131, *supra*, pp. 6, 23, 31, 49 - 50, 51; *and see* Jt. App. 52 n.14.

Further, the district court properly obeyed still another important rule of statutory construction, implicitly agreeing that "[w]here legislative history is inconclusive, it should not be relied upon to supply a provision not expressly in the statute." *Beyer* v. *C.I.R.*, 916 F.2d 153, 157 (4th Cir. 1990), citing *United States* v. *American College of Physicians*, 475 U.S. 834, 846 (1986).

Finally, the district court faithfully heeded the warning of the Supreme Court that an "attempt at the creation of legislative history through the *post hoc* statements of interested onlookers is entitled to no weight." *Western Air Lines* v. *Board of Equalization*, 480 U.S. 123, 130 - 131 n. * (1987). Thus, the district court was unpersuaded by defendant's efforts to

[13] *Compare id.*, at 51 ("Nothing in the Act . . . . board of trade.") with 7 U.S.C. § 2 (Treasury Amendment).

shift the interpretive focus from the language of the statute to interpretations fashioned after passage of the Act, which were at variance with the language of the Act. *See*, *e.g.*, Jt. App. 53 - 54 n.15.[14]

In sum, the district court properly began with the language of the statute itself. Jt. App. 49, 50. Then, finding that the language unambiguously did *not* limit exclusion from the coverage of the CEA on the basis of the nature of the participant in the transaction, Jt. App. 50, the district court reviewed the legislative history in search of a "clear, unambiguous basis for concluding, as [defendant] insists, that 'transactions in foreign currency' contains a limitation on the transactional participants." Jt. App. 51. Then the court correctly found that "the legislative history reveals no [such] clear unambiguous expression of legislative intent to restrict the Treasury Amendment." Jt. App. 53.

The conclusion is ineluctable, therefore, that the district court was correct, when concluding:

> Applied here, these well-established principles of statutory interpretation compellingly point to the conclusion that the foreign currency contract between [defendant] and [plaintiff] are covered by the Treasury Amendment .... Simply put, in the CEA context, the phrase "transaction in foreign currency" plainly and unambiguously means any transaction, without limitation as to the participants involved, in the commodity or subject matter ....

Jt. App. 50.

This Court should, therefore, affirm the district court's interpretation of the Treasury Amendment.

2. Defendant's attempt to fashion a new statutory interpretation is wholly without merit.

While defendant sought unsuccessfully to persuade the district court that the Treasury Amendment should be interpreted as if it "contains a limitation on the transactional participants," Jt. App. 51, he now requests from this Court a *different*, and unlikely, interpretation of the Treasury Amendment — to wit, that the Amendment was *not* intended to exclude foreign currency futures and options from the coverage of the CEA, and from the regulatory authority of the CFTC. Rather, defendant *now* argues, the Treasury Amendment, and, therefore the "provision" submitted by the Treasury Department, *see*, S. Rep. No. 93-1131, *supra*, at 49, was intended to exclude *only* "a 'spot' transaction — which involves an immediate sale and conveyance — [and] a 'cash forward' transaction, which also involves a present sale, with delivery merely deferred though fully expected." Brief for Appellant, p.14. As defendant now puts it, "only these . . . transactions, in which the parties buy and sell, and plan conveyance of, the actual commodity, the Treasury Amendment covers." *Ibid.*; *and see*, *id.*, pp. 13 - 32.

This new interpretation is insupportable. First, the entire import of the CEA, since its origin in the Future Trading Act, 42 Stat. 187 (1921), and in every subsequent version of the statutory scheme, has been to "oversee the volatile and esoteric *futures* trading complex." *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Curran*, 456 U.S. 353, 356 (1982) (emphasis supplied). Thus, the various statutes have *always* excluded from the overall regulatory scheme transactions which defendant now describes as being uniquely excluded by the Trea-

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[14] In any event, the Treasury Department's statutory interpretation has been in precise accord with the district court's interpretation of the reach of the Treasury Amendment. Compare, *e.g.*, Jt. App. 56 - 57 ("All transactions in which foreign currency is the actual subject matter of an off-exchange contract for future delivery are exempt from the CEA.") *with* Letter of Charles O. Sethness, Assistant Secretary of the Treasury, May 5, 1986, ("By its terms, the Treasury Amendment exemption is a transactional one that places outside the coverage of the Act "all off-exchange future transactions in the listed financial instruments."), forwarding Comments of Treasury Department in Response to "Commodity Futures Trading Commission, Trading in Foreign Currencies for Future Delivery, Statutory Interpretation and Request for Comments," 50 Fed. Reg. 42983 (October 23, 1985). (For the convenience of the Court, a copy of the Treasury Response of May 5, 1986, is attached as an Addendum).

sury Amendment — that is, transactions "in which the parties buy and sell, and plan conveyance of, the actual commodity." Brief for Appellant, p. 14.

Indeed, the sentence immediately following the Treasury Amendment in the current version of the CEA is the present-day version of that ever-present exclusion:

> The term "future delivery," as used in this chapter, shall not include any sale of any cash commodity for deferred shipment or delivery.

7 U.S.C. § 2.[15] Common sense dictates the conclusion that Congress could not have intended the Treasury Amendment to exclude only spot and cash forward transactions, as defendant now argues, when the very next sentence of the present statute — a sentence which antedated the Treasury Amendment — does, and has always done, precisely that.

Defendant purports to support this remarkable argument by resorting to a variety of efforts to reduce the Treasury Amendment to ambiguity, and then to create out of whole cloth a legislative "history" dedicated to the notion that Congress meant to exclude only spot and cash forward transactions by both the Treasury Amendment *and* the immediate next sentence. These arguments need not be addressed in detail here, as they all fall before two simple truths. First, the CEA's design to "oversee . . . *futures* trading," *Curran*, *supra*, dictates that, in the first instance, an *exclusion* from the Act's coverage would be an exclusion of "futures" transactions.[16]

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[15] This exclusion is ordinarily referred to as the "cash forward" exclusion.

[16] The "cash forward" exclusion itself originated, in the 1921 Future Trading Act, out of concern over assuring the legitimacy of cash grain contracts between farmers and grain elevator operators for the *future* delivery of grain. *See* Hearings on H.R. 5676 Before the Senate Committee on Agriculture and Forestry, 67th Cong., 1st Sess. 8 - 9, 213 - 214, 431, 462 (1921). The present expression, unchanged since the adoption of the CEA in 1936, by referring to "any cash commodity for deferred shipment or delivery," 7 U.S.C. § 2, retains, for cash forward transactions, this sense of future delivery, while also excluding spot transactions as "cash commodity" sales.

Accordingly, those transactions excluded by the Amendment would plainly include "futures" transactions, unless there were a clear and unambiguous basis in the legislative history for concluding otherwise. As shown above, however, there is no such basis.

Rather, the legislative history clearly and unambiguously establishes the second truth which defendant ignores — that the Treasury Amendment was proffered and enacted to "exempt[ ], from regulation by the Commission, foreign currency *futures* trading . . . ." S. Rep. No. 93-1131, *supra*, p. 49 (emphasis supplied); *see also id.*, p. 51 ("we strongly urge the Committee to amend the proposed legislation to make clear that its provisions would not be applicable to *futures* trading in foreign currencies or other financial transactions . . . described above") (emphasis supplied).

Accordingly, the interpretation of the Treasury Amendment defendant has now offered this Court should be rejected, and the district court's adopted.

Defendant also seeks to support his argument that futures and options contracts in foreign currency are not "transactions *in* foreign currency" within the meaning of the Treasury Amendment through reliance upon language in *Board of Trade of the City of Chicago* v. *Securities and Exchange Commission*, 677 F.2d 1137, 1154 n.33 (7th Cir. 1982), *judgment vacated as moot and remanded with directions to dismiss*, 459 U.S. 1026 (1982) and *Commodity Futures Trading Commission* v. *American Board of Trade, Inc.*, 803 F.2d 1242, 1248 (2d Cir. 1986). However, those decisions rest upon a mistaken interpretation of the Treasury Amendment according to which options on foreign currency or government securities, absent exercise, are not deemed "transactions in," but only as involving or relating to, a commodity. The majority's reasoning in *Board of Trade of the City of Chicago* — which *American Board of Trade* simply assumed was valid — can-

not be reconciled with the statutory purpose of the Amendment.[17]

In petitioning the Supreme Court for review of the Seventh Circuit's decision, the Solicitor General asserted that the court incorrectly interpreted the Treasury Amendment, stating that options on government securities were within the Amendment's "transactions in" language.[18] Congress itself overruled the outcome of *Board of Trade of the City of Chicago* in enacting the Accord Amendments discussed previously (*supra*, n. 7).[19] Following Congress's rejection of the Seventh Circuit decision, the Supreme Court vacated it as moot, and directed the action dismissed, thereby depriving *Board of Trade of the City of Chicago* of further precedential authority.

This Court, however, need not address the correctness of *Board of Trade of the City of Chicago* or *American Board of Trade* because, as the district court found, J.A. 54, even under the "semantical" distinction made in those decisions, the options contracts nonetheless fell within the exclusion of the Treasury Amendment.

The district court correctly pointed out that both *Board of Trade of the City of Chicago* and *American Board of Trade* are in agreement on one important point — a transaction "be-

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[17] Indeed, the dissent in *Chicago Board of Trade* made precisely that point, noting that "[t]he majority's suggestion that 'transactions in . . . government securities' covers only transactions in which the underlying securities change hands [is] flatly contradicted by the structure of [the Treasury Amendment]." *Id.*, 677 F.2d at 1178 - 1179 (Cudahy, J., dissenting) (ellipsis in original).

[18] *See* Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit, *Securities Exchange Commission* v. *Board of Trade of the City of Chicago*, No. 82-526 (S. Ct.), at 21 & n. 21.

[19] *See* H.R. Rep. No. 626, 97th Cong., 2d Sess. 7 (1982) ("The dissenting opinion (Cudahy) noted that the majority's decision reflected a 'bizarre' and 'extreme' conclusion. The Committee believes the court's decision is not consistent with long-standing Congressional intent that the SEC has the sole authority to regulate options on all securities, including exempted [*e.g.*, government] securities.").

comes one 'in' foreign currency," once the subject contract is exercised, as were the contracts in question in this case. J.A. 55. Defendant does not disagree at this time, nor does he argue here that a triable issue of fact exists as to whether the contracts were exercised. Rather, defendant's argument related to the exercise of the contracts is his contention that, without delivery of the currency itself, the subject contracts could not be considered "exercised." Brief for Appellant, p. 21 n.13.

However, this argument ignored settled law, and has no real impact upon the conclusion reached by the district court. As the district court reasoned, the parties substituted "offsetting transactions [for the] actual receipt or delivery of [the] foreign currency." Jt. App. 55. The court then concluded that this "set-off is, in legal effect, a delivery." *Ibid.*, citing *Board of Trade* v. *Christie Grain & Stock Co.*, 198 U.S. 236, 248 (1905). Such delivery, the court concluded, is exercise of the subject contracts causing them, at that time, even if, *arguendo*, not before, to be "transactions in" foreign currency.

Thus, even accepting, for the purpose of argument, the interpretation of the Treasury Amendment fashioned in *Board of Trade of the City of Chicago* and *American Board of Trade*, *supra*, the subject transactions were "transactions in" foreign currency, and, therefore, subject to the exclusionary force of the Treasury Amendment.

CONCLUSION

For the foregoing reasons, this Court should affirm the district court's interpretation of the Treasury Amendment.

Respectfully submitted,

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AUGUST 1992

ADDENDUM

Letter of Charles O. Sethness, Assistant Secretary of the Treasury, May 5, 1986, forwarding Comments of Treasury Department in Response to "Commodity Futures Trading Commission, Trading in Foreign Currencies for Future Delivery, Statutory Interpretation and Request for Comments," 50 Fed. Reg. 42983 (October 23, 1985).

DEPARTMENT OF THE TREASURY
WASHINGTON

May 5, 1986

ASSISTANT SECRETARY

Dear Chairman Phillips:

As you know, an existing provision of the Commodity Exchange Act known as the Treasury Amendment provides an exemption for off-exchange futures transactions in foreign currency, government securities and certain other financial instruments. The interpretative statement concerning this Amendment that was published for public comment late last year by the Commodity Futures Trading Commission (the "Commission") would limit the overall scope of the exemption in an effort to eliminate the marketing to the general public of off-exchange futures transactions in foreign currency. See 50 Fed. Reg. 42,983 (1985).

While we agree that it may be appropriate to bring some foreign currency futures transactions marketed to the general public off-exchange within the scope of the Commodity Exchange Act (the "Act"), the possibility that the same narrow interpretation of the Treasury Amendment might be applied to transactions in government securities is of concern to Treasury. The issue was mentioned to Ken Raisler, the Commission's General Counsel, earlier this year in an informal discussion of the Commission's interpretative statement. Our concern has increased substantially because we recently learned that the Commission plans to refine its earlier interpretation of the Treasury Amendment and republish it in the near future, in spite of numerous negative comments received from the public.

By its terms, the Treasury Amendment exemption is a transactional one that places outside the coverage of the Act all off-exchange futures transactions in the listed financial in-

struments. In its interpretative statement, the Commission would limit the exemption to transactions between sophisticated and informed institutions. However, the Treasury Amendment itself contains no language limiting the coverage of the exemption based upon the characteristics of participants in a transaction.

Although the Commission has stated in its recently published release that it "deals only with that portion of the Treasury Amendment which refers to transactions in foreign currency," the analysis of the interpretation logically could extend to transactions in government securities as well as all the other financial instruments listed in the Treasury Amendment.[20] If so extended, it would conflict with a basic goal of Treasury's current legislative proposal that Treasury be the centralized rule making authority in regulating the government securities market.

Because we believe that the Commission's interpretation is not consistent with the plain language of the statute, the appropriate way to permit the regulation in the area of foreign currency transactions is to amend the exemptive provision to redefine its scope with respect to transactions in foreign currency. Although Treasury has no basic objection to bringing within the scope of the Act only the foreign currency transactions of concern to the Commission, we do believe that the Commission's jurisdiction should be defined in such a way that it does not prohibit legitimate hedging transactions entered into by businesses and individuals.

We understand that Congress currently has under consideration legislation that would make a number of amendments to the Act, including at least one amendment that would resolve a question as to the scope of the Commission's power to prevent fraudulent off-exchange futures contracts. We believe

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[20] We note that the interpretative release makes clear that forward contracts will continue to fall outside the scope of the Act. However, the line between futures contracts and forward contracts is not a precise one.

the current bill also is an appropriate vehicle for resolving the issue described above, and we recommend that a provision be added to the bill to make that change. Given our interest in the continued efficient operation of the markets for both foreign currency and Treasury securities, we would be happy to work with you and your staff in crafting a proposed amendment on this issue to be forwarded to the appropriate Congressional committee.

Sincerely,

Charles O. Sethness

Charles O. Sethness
Assistant Secretary
(Domestic Finance)

Ms. Susan M. Phillips
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CERTIFICATE OF SERVICE

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